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December 12, 2001

Honorable Board of Supervisors
County of Orange
Santa Ana, California

Your Honorable Board:

The Comprehensive Annual Financial Report of the County of Orange, State of California, for the fiscal year ended June 30, 2001, is hereby submitted in accordance with the provisions of Sections 25250 and 25253 of the Government Code of the State of California. Responsibility for both the accuracy of the data, and the completeness and fairness of the presentation, including all disclosures, rests with the County. To the best of our knowledge and belief, the enclosed data are accurate in all material respects and are reported in a manner designed to present fairly the financial position and results of operations of the various funds and account groups of the County. All disclosures necessary to enable the reader to gain an understanding of the County's financial activities have been included.

Copies of this Comprehensive Annual Financial Report, the County Proposed and Final Budgets, booklets specifying the tax rates and assessed valuations of taxing agencies in Orange County, and financial reports of certain funds or functions for which the County has fiduciary responsibility, may be obtained from the office of the County Auditor-Controller.

The Comprehensive Annual Financial Report is presented in three sections: Introductory, Financial, and Statistical. The Introductory Section includes this transmittal letter, the County's organizational chart and a list of principal County officials. The Financial Section includes the general purpose financial statements, and the combining and individual fund and account group financial statements and schedules, as well as the independent auditor's report on the financial statements and schedules. The Statistical Section, which is unaudited, includes selected financial and demographic information.

The County is required to undergo an annual single audit in conformity with the provisions of the Single Audit Act Amendments of 1996 and the U.S. Office of Management and Budget Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations." Information related to this single audit, including the Schedule of Expenditures of Federal Awards, findings and questioned costs, and the independent auditor's report on internal control and compliance with applicable laws and regulations, are included in a separate annual publication.

This report includes all funds and account groups of the County, as well as its component units. Component units are separate legal entities for which the County is considered to be financially accountable. The County provides a full range of general government services, including police protection, detention and correction, public assistance, health and sanitation, recreation, library, flood control, waste management, airport management, and general financial and administrative support.

Blended component units, although legally separate entities, are, in substance, part of the County's operations, and therefore data from these units are combined with data of the County. The County has one component unit, the Orange County Children and Families Commission (OCCFC), which requires discrete presentation in the general purpose financial statements for the fiscal year ended June 30, 2001. The following entities are presented as blended component units in the general purpose financial statements for the fiscal year ended June 30, 2001: the Orange County Flood Control District, Orange County Development Agency, Orange County Housing Authority, Orange County Civic Center Authority, Orange County Financing Authority, Orange County Special Financing Authority, Orange County Public Financing Authority, Orange County Public Facilities Corporation, and certain special districts.

Economic Condition and Outlook

Area Population

With a population of over 2.9 million, Orange County is one of the major metropolitan areas in California and the nation. Orange County represents the second most populous county in the state, and ranks fifth in the nation. Population growth exceeded that of the state (2.02% vs. 1.79%).

Area Economy

Orange County represents one of the major economic centers in the state and nation. If Orange County were a nation, its economy would rank 32nd among all the countries in the world, above such countries as Greece, Israel, and the Philippines. The Anderson Center for Economic Research at Chapman University estimates its Gross County Product (GCP) at \$133.0 billion during 2001.

Orange County government has emerged from bankruptcy with a solid recovery plan in effect. Housing price appreciation has returned, with double-digit appreciation evident in certain areas of the County. The County also continues to be represented by a solid economic base in construction, non-durable goods, retail trade and services. It should be noted that a significant sector of the local economy is dependent upon international trade. Therefore, while the forecast for the local economy remains bright, any significant slowdown in the economies of our international trading partners will continue to influence the County's overall level of economic growth.

Unemployment Rate and Tax Base

Orange County's unemployment rate, which reflects the number of unemployed County residents as a percent of the labor force, remains one of the lowest among California counties. As of September 2001, the unemployment rate stood at 3.2%. This compares favorably to rates of 5.8% for neighboring Los Angeles County, 5.2% for California, and 4.7% for the nation.

After an extended period of a depressed real estate market, Orange County's housing sales and prices have continued their rebound. This is reflected in the value of Orange County's tax base. Total assessed valuation increased by \$20.4 billion, or 8.9% over FY 2000-2001 reaching \$ 248.9 billion in FY 2001-2002.

Recent Industry Employment Trends and the Local Economy

Despite the tight housing market, monthly wage and salary employment statistics released by the State Employment Development Department (EDD) estimate the number of jobs located in Orange County will increase regardless of where the employee resides. The latest wage and salary employment estimates from EDD illustrate the County's strong economic base, despite very clear slowing patterns. Total nonfarm jobs in the County reached 1,433,800 in September 2001, reflecting a 0.5% increase over the 1,401,000 jobs in September 2000—an increase of 32,800 nonfarm jobs. Employment in the trade sector recorded gains of 5,700, led by wholesale trade with 3,000 jobs. Manufacturing employment was up by a net of 1,700, led by the durable goods sector with 1,000 jobs. Employment in the services sector increased by 14,500 led by business services with 6,000 jobs. Other significant major nonfarm industry categories with job gains included construction (up 3,900); transportation and public utilities (up 900); finance, insurance and real estate (up 3,400) and government (up 2,400). Mining employment remained relatively unchanged over the year (reflecting an increase of 100 jobs).

County Median Family Income

According to the Anderson Center for Economic Research at Chapman University, Orange County's median family income is estimated at \$71,200 for the year 2001. Projections for the year 2002 are not available at this time; however, it is expected that increases in median family income for 2002 will be moderate due to the slowing of the national, state and local economy.

Impact of September 11, 2001 Terrorist Attacks on State and Local Economy

One word describes the effect of the September 11, 2001 attacks on the economy – uncertainty. There is, at the national, state and local level, a sense of uncertainty about how pervasive the effects will be, how long the effects will remain, whether subsequent events are on the horizon and what their effects might be, and what steps can be taken to pull the economy out of recession. Preliminary indicators show a loss of consumer confidence and spending and a decline in employment. However, how long these effects will last, to what extent these effects will influence other sectors of the economy, and what changes are needed to restore consumer confidence and spending is very much unclear. For now, economists at Chapman University have advised that projections about the anticipated course of the state and local Orange County economy that were generated prior to September 11, 2001 should be maintained, but monitored closely to determine if revisions to the projections will be required. Therefore, the County Executive Office is monitoring General Purpose Revenue projections on a monthly basis.

Bankruptcy Recovery

On December 6, 1994, the County of Orange filed for protection under Chapter 9 of the United States Bankruptcy Code as a result of substantial losses in the Orange County Investment Pool. The liquidation of the Pool's portfolio resulted in the realization of an investment loss of approximately \$1.6 billion, approximately \$600 million of which was allocable (on a pro rata basis) to the County's accounts, with substantially all of the remainder allocable to accounts of non-County Pool participants, such as cities, school districts and special districts.

The County's bankruptcy was the largest municipal bankruptcy ever. After a period of about eighteen months, the County's comprehensive recovery plan was approved by the Federal Bankruptcy Court and the County emerged from the bankruptcy on June 12, 1996. The County's recovery from bankruptcy was in large measure due to the implementation of a strong County Executive Officer (CEO) concept of corporate management, unique among California counties. The corporate management system, which incorporated a fundamental restructuring of the core County government, implementation of annual business plans, and a long range strategic financial plan, has resulted in a fiscally viable County that received a series of upgrades by the three principal rating agencies rating municipal debt, resulting in the County's current ratings: Moody's: Aa2, Fitch IBCA: AA-, and Standard and Poor's: A.

The recovery has not been without significant cost, namely a debt burden of over \$1 billion. Recognizing the need to reduce this burden in order to free up scarce General Fund dollars for more productive uses, the Board of Supervisors has made early debt reduction a high priority. Consequently, as unanticipated revenues have become available, the Board has directed that most of the money be dedicated to early debt reduction. As a first step, in June 1998, about \$31 million in bankruptcy related debt was removed from the books through a legal defeasance of a portion of the 1995 Refunding Recovery Bonds. The County then used its share of litigation proceeds from the bankruptcy-related litigation to assist in the retirement or defeasance of \$317 million of Pension Obligation Bonds.

Major Initiatives for Fiscal Year 2000-2001

Fiscal Year 2000-2001 General Fund Budget

Total discretionary funding for the County's Fiscal Year 2000-2001 Final Budget was \$454.5 million. This included fund balance available of \$86 million unreserved/undesignated, cancellation of the \$35.1 Strategic Priority Reserve and general purpose revenues of \$333.4 million. The general purpose revenues increased by \$22.2 million, or about 7.0% over Fiscal Year 1999-2000. The increase resulted from growth in property taxes and motor vehicle license fees. Total discretionary funding after adjustment for the Strategic Priority Reserve cancellation was within 1.5% of the amount projected in the 2000 Strategic Financial Plan.

The Fiscal Year 2000-2001 Budget funded all the strategic priorities approved by the Board in the 1998 and 1999 Financial Plan; no new strategic priorities were approved in the 2000 plan. The Strategic Priorities funded in the Fiscal Year 2000-2001 budget included:

- Increase to the Debt Prepayment Fund of \$5 million
- Provide \$12.4 million to projects to remedy Deferred Maintenance and Americans with Disabilities Act deficiencies
- Completion of Theo Lacy Branch Jail expansion with a cost of \$10.4 million
- \$4 million to improve Juvenile Detention Facilities
- Increase in Provision for Contingencies by \$1 million for a total of \$22 million

The County's share of the national litigation settlement with major tobacco companies was the subject of controversy during Fiscal Year 2000-2001. The issues were resolved when an initiative ordinance, Measure "H", was approved by the voters on November 7, 2000. This initiative requires that all Tobacco Settlement Revenues (TSR) received after July 1, 2001 are to be allocated 80% to new or expanded health care programs and 20% for public safety.

For Fiscal Year 2000-2001, the County's TSR was not governed by Measure "H", and was allocated by the Board of Supervisors on December 5, 2000, to the following projects:

• Health Care Priorities	\$12,970,000
• Water Quality Testing Laboratory	1,230,000
• Secured 64-Bed Substance Abuse Program	1,330,000
• Theo Lacy Jail Expansion Engineering	5,400,000
• Debt Reduction	<u>7,500,000</u>
	\$28,430,000

The Fiscal Year 2000-2001 Budget was adjusted in February 2001 to reflect the TSR allocation.

Negotiations with Employee Bargaining Units

Negotiations with the Orange County Employees Association (OCEA) and the American Federation of Labor-Congress of Industrial Organizations (AFL-CIO) bargaining units concluded in June 2001, and resulted in 3 year Agreements through June 2004. The new Memorandum of Understanding (MOU) provides for general salary increases of 4% in the first and second years of the contract, and 3.5% in the third year, with an option in the third year for some of the bargaining units to receive a 3.5% retirement contribution in lieu of the general salary increase. Non base building Performance Incentive Program (PIP) performance incentives will continue in each year of the contract, funded in the amount of 2% of base salary per year.

The MOU for the Association of Orange County Deputy Sheriffs (AOCDS) expired in October 1999. Negotiations with this labor organization concluded in October 1999 and resulted in a three-year Agreement, which will expire in October 2002. This Agreement provides for a 3.5% or 3.75% increase for specific classifications in the first year of the Agreement, a 4% increase for all classifications in the second year of the Agreement, and fully paid retirement in the third year of the Agreement.

In 1999, the State passed Assembly Bill 1937 giving Public Employees Retirement System (PERS) and 1937 Act Retirement Plans (which includes Orange County's Retirement System) the option to offer a new benefit formula known as 3% at 50 for public safety members. The AOCDS requested a contract re-opener to discuss this benefit. Based on market research and the need to maintain competitiveness in the public safety labor market, the County Board of Supervisors amended the Personnel and Salary Resolution on December 4, 2001 implementing a 3% at 50 retirement formula for public safety employees effective June 28, 2002. The initial estimated annual cost of this benefit is \$14.7 million and will be funded by a combination of existing Public Safety Sales Tax, law enforcement contract revenue, contributions from the public safety employees and from the County General fund. Costs of this benefit have been included in the County's 2002 Strategic Financial Plan.

The MOU for the Orange County Attorney's Association (OCAA) expired in June 2000. Negotiations with this labor organization concluded in June 2000 and resulted in a three year Agreement which will expire in June 2003. This Agreement provides for a 4% general wage increase in the first and second year of the Agreement and a fully paid retirement in the third year of the contract. Additionally, 1% non-base building performance pay incentives are available in each year of the Agreement. The pay out of incentives will be made in accordance with the jointly developed PIP.

The cost of salary increases has been included in the County Strategic Financial Plan.

Major Initiatives for the Future

Retirement Rate Agreement

The Board and the Orange County Employees' Retirement System (OCERS) Board signed an agreement in 1996 for the use of \$318 million in pension obligation bond proceeds. The proceeds from the bonds were placed in an investment account within OCERS, for the sole purpose of paying County annual obligations for retirement. The investment account is credited with market earnings of OCERS and debited according to a formula that considers available balance and obligations. The investment account balance as of June 30, 2001 was \$241.6 million (unaudited).

The County is required to pay any retirement costs not paid by the investment account. The investment account was originally projected to pay 75% of the County's retirement costs in FY 2000-2001; however, due to higher than anticipated investment earnings, the County's \$45.9 million retirement cost was paid entirely by the investment account.

Marine Corps Air Station El Toro

In 1993, the Defense Base Realignment and Closure Commission directed the closure of Marine Corps Air Station (MCAS) El Toro ("El Toro" or "the base") effective July 1999. In April 1995, the County was designated by the Federal government as the Local Redevelopment Authority (LRA) for the base. As the LRA, the County is responsible for preparing and implementing a "Community Reuse Plan" for transition of the 4,700 acre base to civilian uses. The Federal government encourages the development of Community Reuse Plans which facilitate local economic redevelopment, job creation and timely environmental cleanup.

In December 1996, the Board of Supervisors (Board), acting as the LRA, adopted a final MCAS El Toro Community Reuse Plan, approved the Homeless Assistance Submission, and certified the supporting Environmental Impact Report (EIR). The Community Reuse Plan was subsequently submitted to the Department of Navy for consideration. When the Community Reuse Plan was adopted, the Board directed the CEO to initiate the next phase of planning for the base, specifically, the preparation of a Planned Community/Specific Plan for the entire base and an Airport System Master Plan addressing aviation services and facilities at both El Toro and John Wayne Airport, Orange County. The Marines vacated the base in June 1999.

The County retained consultant teams to prepare the Airport System Master Plan and EIR 573. These plans, undertaken by the El Toro Local Redevelopment Authority, together with federal environmental documents, will form the basis for recommendations regarding to whom, and by what means, base property should be conveyed. It is anticipated that much of the base will be requested by and conveyed to the County, which will then serve as a "master developer" of the site. The County's role will extend over many years, and can be characterized in two primary phases: (1) Planning (2) Maintenance and Implementation. The Planning Phase was completed on October 23, 2001. During this phase, the Airport System Master Plan and a second EIR were completed and approved by the Board. The County's Maintenance and Implementation Phase includes maintaining base facilities, and interim leasing of selected base facilities. The County signed a five-year Master Lease with the Department of the Navy in September 2000 under which these activities are being conducted.

The Orange County Central Park and Nature Preserve Initiative (Measure W) has been certified by the County Registrar of Voters and on December 4, 2001, the Board of Supervisors placed the initiative on the March 5, 2002 ballot. The initiative would amend the Orange County General Plan and restrict the types of land uses on County-owned land within unincorporated County territory at MCAS El Toro. If passed by the voters, Measure W would repeal a previously adopted measure, Measure A, which designated much of MCAS El Toro for civil aviation and related uses and limit El Toro to what is described as "education compatible" uses and "open space reserve" uses allowing for facilities typically funded by the public sector, such as a park, library, museum, and zoo. The initiative is the subject of ongoing litigation. A Superior Court judge invalidated the initiative. Thereafter, the Court of Appeals reversed the judge's decision. Opponents of the initiative have filed for review by the California Supreme Court.

Santa Ana River Mainstem Project

The Santa Ana River Mainstem Project and the proposed Prado Dam Project are major flood control projects, which when fully completed, are designed to prevent the type of devastating damage caused by large-scale flooding that occurs on the average of every 190 years in the Santa Ana River flood plain. The projects involve a combination of flood channel widening and reinforcement, construction of a new dam, Seven Oaks Dam, and raising the existing dam, Prado Dam.

The Federal government, Orange County Flood Control District (OCFCD), San Bernardino County Department of Transportation/Flood Control District, and Riverside County Flood Control and Water Conservation District are cost sharing the U.S. Army Corps of Engineers' (COE) estimated total project cost of \$1.4 billion. The OCFCD currently estimates its share of costs for the two projects to be \$413 million for acquisition of real property rights for construction of the project, relocation of designated roads, bridges, trails, channels and utilities, and construction cost share contributions.

OCFCD's remaining share of project costs exceeds current available funds. However, the project has been authorized by the State Legislature, making it eligible for State Flood Control Subventions (reimbursement of 70% of OCFCD expenditures). An estimated \$54 million in budgeted or encumbered funds are expected to be reimbursed to the OCFCD over the next 18 months by the State Department of Water Resources. As of June 30, 2001 the OCFCD spent an estimated \$203 million on the projects, with resulting claims for reimbursement of \$140 million which have already been or will be submitted over the next 18 months. To date, the OCFCD has claimed \$132.5 million of eligible expenditures and received \$94 million in reimbursements.

Strategic/Financial Plan

The County Executive Office prepares an annual Strategic Financial Plan (Plan) which is an integral part, along with departmental business plans and the budget, of the corporate management system. The Plan consists of an economic/revenue forecast provided by Chapman University and operational spending forecasts provided by each County department. The purpose of the Plan is to:

- Provide a long range financial context for program and infrastructure decisions
- Demonstrate the viability of the County's baseline operations
- Identify potential financial challenges
- Identify opportunities to fund new "strategic priorities" (e.g. jail expansion)
- Provide the framework for budget policies

In June 2001, the Board approved a new Debt Reduction Policy. The next target for debt reduction is the 1995 Recovery Bonds issue. However, the low interest rate environment as of October 2001 was not favorable to funding defeasance escrows. As of October 2001, the Board has set aside \$92.4 million for debt reduction with plans to add about \$10 million per year for the next four years.

On October 30, 2001 the Orange County Board of Supervisors adopted the 2002 Strategic Financial Plan. The Plan provides a very constrained outlook over the coming years and projects no additional available funding for new strategic priorities. The early years of the Plan include surpluses that have been used to balance the forecast along with funds from the Strategic Priority Reserves. However, the Plan shows that beginning with fiscal years 2007-08, baseline operations in combination with priorities approved in previous years are forecast to outstrip available resources. The County Executive Office will monitor revenue and cost data on a periodic basis, provide updates to the Board of Supervisors, and propose measures to produce a balanced outlook with respect to revenue sources and baseline expenditures.

Department Focus

Orange County Public Library

The advent of the internet and improvements in information technology have transformed the service program of the Orange County Public Library. At twenty-seven branch libraries, County residents log on for over 200,000 hours of internet access annually. The Library website, which offers interactive customer services, is visited by over 250,000 persons per year on a twenty-four hour per day, seven days a week basis. Utilizing State grant funds and in cooperation with other Southern California libraries, the Orange County Public Library also offers online, live "chat" format reference assistance on an individual basis to library users.

Technological improvements have also allowed the public to make greater use of the Library's print materials collection. Online consultation of the entire 2.5 million item library catalog and the opportunity to request any book from any library in the System have contributed to all time high records of items borrowed by residents, totaling over 6,260,000 loans in Fiscal Year 2000-2001.

Budgetary Controls

The County maintains budgetary controls to ensure compliance with legal provisions embodied in the annual appropriated budget approved by the Board. Activities of the General Fund and most of the special revenue, debt service, and capital projects funds are included in the annual appropriated budget. The level of budgetary control (that level which cannot be exceeded without action by the Board) is the fund-agency unit level, which represents a department or an agency. The County also maintains an encumbrance accounting system as one technique of accomplishing budgetary control. Encumbered appropriations do not lapse at year-end; encumbrances outstanding at that time are reported as reservations of fund balance for the following year's budget.

Financial Information

Management of the County of Orange is responsible for establishing and maintaining internal controls designed to ensure that the assets of the County are protected from loss, theft, or misuse, and to ensure that adequate accounting data are compiled to allow for the preparation of financial statements in conformity with generally accepted accounting principles. Internal controls are designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived from it. The evaluation of costs and benefits requires estimates and judgments by management.

Single Audit

As a recipient of Federal and State financial assistance, the County is also responsible for ensuring that adequate internal controls are in place to ensure compliance with applicable laws and regulations related to those programs. Internal controls are subject to periodic evaluation by management and the Internal Audit Department.

As part of the County's single audit, described earlier, tests are made of the County's internal controls and of its compliance with applicable laws and regulations, including those related to federal awards. The County's single audit for the fiscal year ended June 30, 2001 is in process.

General Government Functions

The following schedule presents a summary of General Fund revenues, other financing sources, and residual equity transfers from other funds for the fiscal year ended June 30, 2001, and increases and decreases in relation to prior year amounts (in thousands):

Source	2000-01 Amount	Percent of Total	Increase (Decrease) from 1999-00	Percent of Increase (Decrease)
Revenues				
Taxes	\$ 200,836	10.5%	\$ 9,459	4.9%
Licenses, Permits, and Franchises	6,853	0.4	30	0.4
Fines, Forfeitures and Penalties	44,365	2.3	6,509	17.2
Use of Money and Property	29,277	1.5	3,589	14.0
Intergovernmental Revenues	1,252,681	65.4	173,910	16.1
Charges for Services	248,113	12.9	14,628	6.3
Other Revenues	69,267	3.6	(8,156)	(10.5)
Other Financing Sources				
Operating Transfers In	59,362	3.1	(21,276)	(26.4)
Proceeds from Capital Lease Obligations	6,544	0.3	(13,141)	(66.8)
Residual Equity Transfers From Other Funds	44	--	(172)	--
Total	<u>\$ 1,917,342</u>	<u>100.0%</u>	<u>\$ 165,380</u>	

The following information provides a brief summary of the primary factors attributable to increases in General Fund revenues:

Intergovernmental Revenues

- Increased federal and state revenues resulting from growth in assistance programs such as California Work Opportunity and Responsibility to Kids (CalWORKs), Medi-Cal, Child Welfare Services, Continuing Care, Domestic Abuse, Independent Living Care and In-Home Supportive Services.
- Increased revenues for health care programs such as Mental Health Realignment, Mental Health Early and Periodic Screening Diagnosis and Treatment (EPSDT), Managed Care, Mentally Ill Offender Crime Reduction, Children System of Care and for Integrated Services Program to Homeless Mentally Ill Clients.
- Increased revenues from motor vehicle license fees due to a continued strong California economy and a rise in automobile sales in FY 2000-01.
- Increase in Proposition 172 revenues distributed by the State arising from sustained increases in taxable sales. Proposition 172, the Public Safety Sales Tax, is a voter-approved measure passed in 1994 establishing a ½ percent (0.5%) sales tax on an ongoing basis for local public safety programs.
- Increase in federal and state funding for the Temporary Assistance for Needy Families (TANF) program to align the State-wide maintenance of effort with the federal government for the funding of this program.
- Increase in child support collections and federal reimbursements of higher cost claims in administering the Title IV-D Child Support Program.

Charges for Services

- Increases in labor costs such as salaries and employee benefits of sworn personnel assigned to court security.
- Addition of a new city (Rancho Santa Margarita) to receive contract law enforcement services along with an increase in usage by other contract cities in additional positions, equipment, overtime and general services.
- Increases in Federal Medi-Cal revenues received for providing new services, as well as expanding existing services such as Children and Youth Services and Adult Mental Health Services.
- Increase in revenues from the Registration and Elections Department. Both the general and the primary elections revenues are on a two-year cycle and the receipt of these revenues occurred in FY 2000-01.

Charges for Services (Cont'd)

- Increased revenues collected from recording a greater number of legal documents in the Clerk Recorder's office. Lower interest rates contributed to a higher number of legal documents being processed and recorded for property sales and mortgage loan refinancing transactions. Recent legislative changes in the priority afforded to aliens married to United States citizens in the issuance of green cards added to the number of marriage licenses being processed in FY 2000-01.
- Increase in direct and indirect reimbursements from building and safety projects due to an increase in planning and development services.
- Increase was partially offset by a decrease in revenues resulting from reductions in fines, fees and forfeitures imposed by the courts.

The following information provides a brief summary of the primary factors attributable to decreases in General Fund other financing sources:

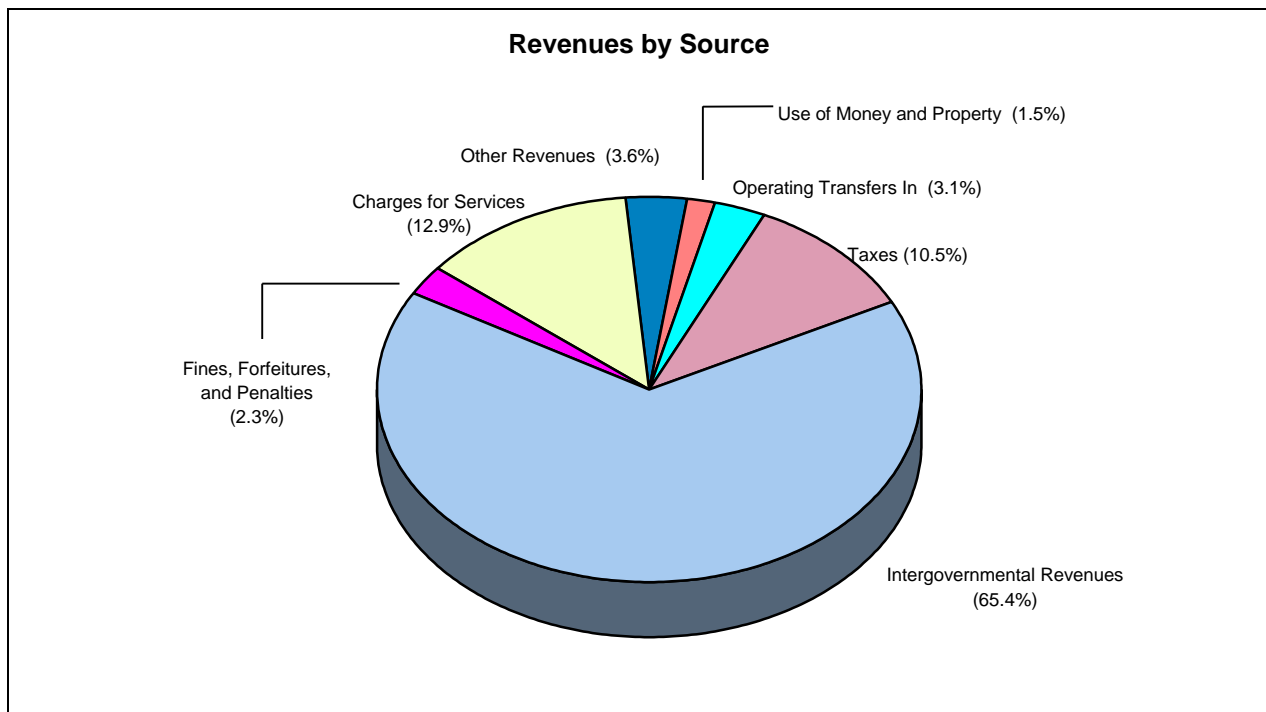
Operating Transfers In

- A decrease in operating transfers attributable to a variety of one-time transfers to the General Fund in FY 1999-00 that did not occur in FY 2000-01.
- Decrease was partially offset by
 - An increase in transfers of Public Sales Tax Excess Revenues (Proposition 172) to the Sheriff's Department to fund capital projects.
 - An increase in transfers of Tobacco Settlement Revenue to the Health Care Agency to address health care priorities as outlined in the Strategic Financial Plan.

Proceeds from Capital Lease Obligations

- Prior year capital lease acquisition of a building for the District Attorney department.

The following diagram shows each revenue source as a percentage of total General Fund revenues. Revenues from Licenses, Permits, and Franchises, Proceeds from Capital Lease Obligations and Residual Equity Transfers from Other Funds are not displayed on the diagram because they represent less than 0.5% of total revenues.



The following schedule presents a summary of General Fund expenditures and other financing uses for the fiscal year ended June 30, 2001, and increases and decreases in relation to prior year amounts (in thousands):

Function	2000-01 Amount	Percent of Total	Increase (Decrease) from 1999-00	Percent of Increase (Decrease)
Current Expenditures				
General Government	\$ 111,635	6.2%	\$ 4,110	3.8%
Public Protection	633,515	35.0	39,802	6.7
Public Ways and Facilities	26,707	1.5	1,973	8.0
Health and Sanitation	352,972	19.6	44,593	14.5
Public Assistance	516,572	28.6	37,085	7.7
Capital Outlay Expenditures	23,612	1.3	(15,670)	(39.9)
Debt Service Expenditures	6,743	0.4	(1,993)	(22.8)
Other Financing Uses				
Operating Transfers Out	133,200	7.4	(26,546)	(16.6)
Total	<u>\$ 1,804,956</u>	<u>100.0%</u>	<u>\$ 83,354</u>	

The following information provides a brief summary of the primary factors attributable to the increases in General Fund expenditures:

Public Protection

- Addition of several new positions in the District Attorney's Criminal and Family Support Divisions, Customer Services Enhancement and Child Support Automated System and at the Sheriff's Department for expanding law enforcement services to various entities combined with increases in cost of living, workers compensation, group insurance and contract costs.
- New positions added in the Probation Department due the implementation of the County's Comprehensive Multi-agency Juvenile Justice Plan and the State's Substance Abuse and Crime Prevention Act of 2000, also known as Proposition 36. The multi-agency plan, approved by the Board in December 2000, addresses the full spectrum of juvenile justice activity including crime prevention, intervention, suppression and programming for incarcerated youth. Proposition 36 is a voter approved measure passed in November 2000 allowing the first and second time, non-violent, simple drug possession offenders the opportunity to receive substance abuse treatment instead of incarceration.
- Increase was partially offset by a reduction in the County's required contribution for the funding of trial court operations as stipulated by Assembly Bill 233 (AB 233). AB 233 is a court reform bill signed in October 1997 to create a stable, long-term funding solution for the trial courts. It requires the State to assume full responsibility for funding trial courts operations and limits the counties' fiscal responsibility.

Health and Sanitation

- Increase in contract services from the Behavioral Health, Emergency Medical Services and Tobacco Settlement funded programs.
- Addition of several new positions in Health Care Agency to support new programs and to expand existing programs such as Children and Youth Services – Children System of Care, Adult Mental Health Services – Integrated Services Program for Homeless Mentally Ill Residents, Alcohol and Drug Abuse Services and Multi-agency Juvenile Justice Plan combined with cost of living increases.
- Increase was partially offset by reimbursements from the Social Services Agency to support their Supportive and Therapeutic Option (STOP) and CalWORKs programs.

Public Assistance

- Addition of new positions and increases in contract services and costs in programs such as CalWORKs, Medi-Cal, Child Welfare Services, Continuing Care, Independent Living Program and In-Home Supportive Services.
- Increase in data services charges and costs for the implementation of the State-mandated CalWORKs Interface Network system (CalWIN).
- Increases in cost of living adjustments to salaries and insurance costs resulting from higher health insurance rates and new positions.
- Increase was partially offset by a reduction in assistance caseloads and related costs for welfare payments to clients in the CalWORKs program.

The following information provides a brief summary of the primary factors attributable to the decreases in General Fund expenditures:

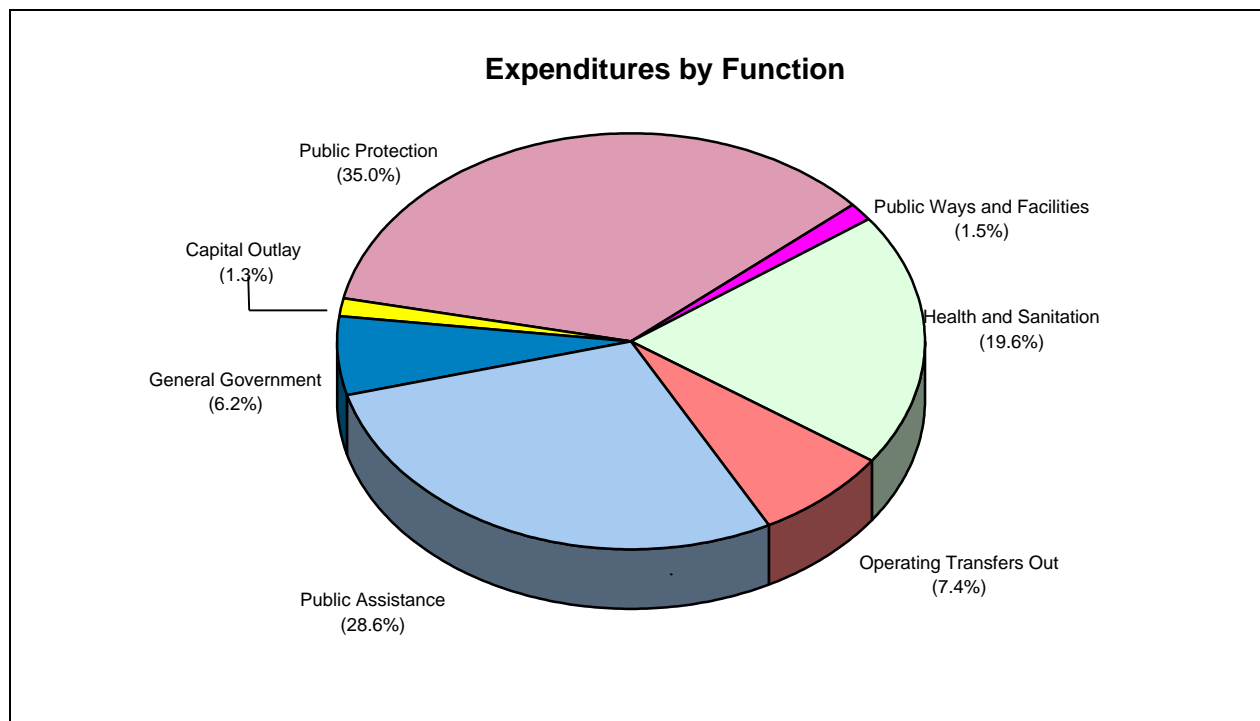
Capital Outlay

- Prior year capital lease of a building for the District Attorney department.

Operating Transfers Out

- A decrease in operating transfers to the Debt Prepayment Fund for the economic defeasance of the Pension Obligation Bonds and to the Sheriff-Coroner Construction and Facilities Development Fund for the Theo Lacy Jail expansion.
- Decrease was partially offset by increased transfers of excess Proposition 172 revenues to the County Public Safety Sales Tax Excess Revenue Fund to finance future projects and by a one time transfer of \$6 million to Shelter Care Facilities Development and Maintenance Fund to finance future strategic priorities, such as providing housing to CalWORKs recipients.

The following diagram shows each category of expenditures as a percentage of total General Fund expenditures. Debt Service Expenditures are not displayed on the diagram because they represent less than 0.5% of total expenditures.



The fund balance of the General Fund increased by approximately \$88.8 million (37.2% increase from FY 1999-00) during the year ended June 30, 2001.

Appropriations Limit

Article XIII B of the California Constitution, as amended by Proposition 111, approved by the voters in June 1990, limits appropriations from the proceeds of taxes. Appropriations are limited to the prior year's amount adjusted by a factor based on population growth and increases in personal income or non-residential assessed value. Proposition 111, in addition to providing greater flexibility in the computation of increases to the appropriations limit, exempts from the limit certain appropriations for fixed assets. The County does not believe it is in danger of reaching its limitation in the next several years.

Enterprise Operations

Airport

John Wayne Airport (JWA) operations are accounted for in an enterprise fund. JWA provides commercial air travel, air cargo, and general aviation services. JWA experienced a decrease of 2.4% in total passenger traffic from FY 1999-2000. The decrease had no significant impact on JWA operating revenues, which remained consistent with the prior year. Operating income at JWA is sufficient to enable the enterprise fund to continue servicing debt and meeting operating costs without support from the County General Fund.

Waste Management

The Integrated Waste Management Department (IWMD) operations are accounted for in an enterprise fund. The Waste Management Enterprise consists of three active landfills, four Household Hazardous Waste Collection Centers, and twenty closed landfill sites. The active facilities provide for the disposal of solid waste, and the collection and disposal of household hazardous waste for Orange County residents. The disposal fees charged to users of disposal facilities are the primary sources of revenue. During Fiscal Year 2000-2001, operating revenues were sufficient to enable the enterprise to service debt and fund operations without support from the General Fund.

The Waste Management Enterprise also imports solid waste in order to provide revenue to the County General Fund for use in meeting County bankruptcy related obligations. During Fiscal Year 2000-2001, IWMD contributed \$14 million of net imported revenue to the General Fund.

Debt Administration

At June 30, 2001, the County had a number of debt issues outstanding. Under current State statutes, the County's general obligation bonded debt issues are subject to a legal limitation based on 1.25% of the total assessed value of real and personal property. As of June 30, 2001 the County had no net general obligation bonded debt. The County's legal debt limit was \$2.9 billion.

Cash Management Policies and Practices

Cash temporarily idle during the year was invested in the Orange County Investment Pools. The Treasurer maintains two separate investment pools, the Orange County Investment Pool (County Pool) and the Orange County Educational Investment Pool (Educational Pool), the latter of which is utilized exclusively by the County's school districts. The investment of the County and Educational Pools is governed by the California Government Code and the Treasurer's Investment Policy Statement (IPS). The IPS is submitted annually to the Treasury Oversight Committee and the Board of Supervisors and authorizes investments in the following categories: U.S. Government securities, securities of federally-sponsored agencies, domestic commercial paper, negotiable certificates of deposit, repurchase agreements, bankers' acceptances, money market mutual funds, State of California or California Municipal debt, receivable-backed securities, and medium-term notes. The IPS prohibits borrowing for investment purposes, reverse repurchase agreements, and volatile structured notes and derivatives. For purposes of determining net asset value of the Funds, investments are marked to market on a daily basis. If the net asset value of either the County Money Market Fund or the Educational Pool is less than \$.995 or greater than \$1.005, portfolio holdings may be sold as necessary to maintain the ratio between \$.995 and \$1.005.

On June 20, 2000, the Board of Supervisors approved a revised IPS with an effective date of July 1, 2000. The new IPS establishes a Money Market Fund and an Extended Fund as components of the County and Educational Pools. The maximum term of any investment under the Extended Fund is three years and the weighted average maturity is limited to 18 months. The maximum term of any investment in the Money Market Fund remains thirteen months with the weighted average maturity limited to 90 days. The Treasurer will determine, based on cash flow projections, the amount of money to invest in the Extended Fund.

In addition to "Pooled Cash/Investments," the Treasurer maintains individual specific investments for certain funds. These amounts comprise a small portion of the total investments managed by the Treasurer. The permitted investments for these funds are dictated by operation of federal or state statute, bond documents, and by mutual agreement with the investing entity.

The County held a portion of its Restricted Cash and Investments with Trustee in the form of non-participating Bank Investment Contracts (BICs). These BICs are considered deposits with financial institutions and amount to \$25.5 million of which \$300,000 was insured by FDIC insurance with \$16.4 million collateralized for non-pooled investments BICs and \$9.1 million uncollateralized for the Restricted Cash and Investments BICs. The remaining portion of the County's deposits are either insured by federal depository insurance or are collateralized with securities having a market value of at least 110 percent of the deposits in accordance with Section 53652 of the California Government Code. Collateral of 150 percent is required if a deposit is secured by first mortgages or first trust deeds upon improved residential real property located in California. Portfolio investments, other than money market mutual funds, are held by a third party custodian in the County's name and are classified in the category of lowest custodial credit risk as defined by the Governmental Accounting Standards Board.

At June 30, 2001, the weighted average maturity of the County Pool was 172 days and the Educational Pool was 79 days. The average daily investment balance of the County Pool and the Educational Pool amounted to \$2.22 billion and \$1.20 billion, with an average yield of 6.25% and 6.07%, respectively, for the fiscal year ended June 30, 2001. The pools managed by the Treasurer have outperformed their designated benchmarks of the 90-day U.S. Treasury Bill and an average of four similar institutional money market funds.

Risk Management

The County has maintained a formal risk management program since the mid 1970's. Risk Management functions include risk identification, measurement, avoidance, loss prevention and mitigation programs, liability transfer (by contract and commercial insurance), risk retention, managing claims and litigation.

Resources are budgeted in the Workers' Compensation and Property, Casualty and Risk Internal Service Funds to pay program costs including losses, expenses and administration costs. Commercial insurance coverage is purchased for the County's property and for certain specialized liability exposures such as airport, dam, helicopter, watercraft, business interruption, crime bond, and notary bonds. All other liability exposures, including general, auto, and workers' compensation, are self-insured. Excess coverage for liability and workers' compensation has also been purchased. Various risk control techniques, including employee accident prevention training and regular work-site inspections, have been implemented to minimize losses. Actuarial studies are performed annually to determine the funding requirements for these activities.

Other Information

Independent Audit

The general purpose financial statements have been audited by the independent certified public accounting firm of Macias, Gini & Company LLP. In addition to meeting the requirements set forth in State statutes, the audit was also designed to meet the requirements of the Federal Single Audit Act Amendments of 1996 and the Office of Management and Budget Circular A-133, "Audits of States, Local Governments and Non-Profit Institutions." The independent auditor's report, on the general purpose financial statements and the supplemental combining, individual fund and account group financial statements and schedules, is included in the Financial Section of this report. The auditor's reports related specifically to the Single Audit will be included in a separate publication.

GFOA Award

The Government Finance Officers Association (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the County of Orange for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2000. The Certificate of Achievement is the highest form of recognition for excellence in state and local government financial reporting.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized CAFR, whose contents conform to program standards. Such a CAFR must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to meet the Certificate of Achievement Program's requirements, and we are submitting it to the GFOA to determine its eligibility for another certificate.

County of Orange Web site

The County of Orange Web site at www.oc.ca.gov provides residents and anyone with internet access, extensive information about County government and the region. With more than 70,000 documents online, the County receives more than 1.5 million hits each month. Featured online are job listings, meeting agendas and County directories. The site provides several online services such as live and archived Board meeting audio, opportunities to comment on Board agenda items, virtual building permit applications and virtual job applications. Also available online are virtual order forms for birth, death and marriage certificates. In addition, the Web site is an excellent source of information on the Board of Supervisors, the Superior Court, assessment appeals, voter registration, elections, homeless prevention and the County's budget.

Acknowledgments

I would like to express my sincere appreciation to the staff from my office, other County departments, and the staff of the certified public accounting firm of Macias, Gini & Company LLP for making possible the timely presentation of this Comprehensive Annual Financial Report. I hope this report will be of interest and use to those in County government, other governmental agencies, and the public interested in the financial activity of the County of Orange.

Respectfully submitted,

original signed by
David E. Sundstrom

David E. Sundstrom, CPA
Auditor-Controller